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Mr Imran Vanker
Director: Standards

12 April 2023

Independent Regulatory Board for Auditors
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Per email: standards@irba.co.za

Comment Letter: Proposed Amendments to the IRBA Code of Professional Conduct - *Revisions to the Definitions of Listed Entity and Public Interest Entity in the IRBA Code*.

Dear Mr. Vanker

We welcome the opportunity to comment on the exposure draft. This comment letter deals with responses to the questions posed in the exposure draft. The comments and considerations expressed in this comment letter are based on collated views of Ernst & Young Inc. in Iouth Africa and do not represent the collective view of the global EY network of firms.

Our comments are structured in two parts:

- Part A: General Comments addresses a short introduction which provides some comments relevant to all the questions you have asked (for avoidance of repetition)
- Part B conforms to your requested format with our detailed answers to your specific questions.

We thank the Independent Regulatory Board for Auditors (IRBA) for an opportunity to contribute to the process. If you wish to discuss these comments further, please contact Roger Hillen (roger.hillen@za.ey.com)

Yours sincerely,

DocuSigned by:
Michael J Schafer
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Roger Hillen
Africa Professional Practice Director

Michael Schafer
Africa Independence Leader

Part A: General Comments

In general, we are supportive of the IRBA Board approving the proposed Revisions to the Definitions of Listed Entity and Public Interest Entity in the IRBA Code to strengthen the requirements contained in the IRBA Code and provide additional guidance to South African audit firms and registered auditors. The proposed IRBA Revisions to the Definitions of Listed Entity and Public Interest Entity provide additional clarity and are expected to result in greater consistency across audit firms in South Africa in terms of classification of PIE audit clients.

We recognise that the proposed IRBA Revisions to the Definitions of Listed Entity and Public Interest Entity in the IESBA Code will require our firm to consider the implications of the revised Public Interest Entity (PIE) definition and the definition of a publicly traded entity when compared to the previous definition of a PIE and a listed entity to ensure that we have appropriately classified our PIE audit clients. Considerations will include the implications of the changed definitions on Mandatory Audit Firm Rotation (MAFR) as set out in the IRBA Rule thereon.

Our detailed comments in response to each of the questions posed in the exposure draft are set out below, which does include our concerns and reservations specific to paragraph R400.18 SA of the proposed revisions to the IRBA Code.

Respondent Information

Respondent type *Please select the capacity in which you are responding.*	Firm
Organisation Name *If you answered "Individual", please write "Private".*	Ernst & Young Inc.
Full Name	• Roger Hillen
Job Title	• Professional Practice Director
Email Address	• roger.hillen@za.ey.com

Question 1: Do respondents agree that the proposed amendments provide useful guidance to help the registered auditor in determining whether an entity is a public interest entity? Yes / No.

If "No", please indicate where additional guidance is needed.

Response to Question 1

a) Yes, we support the proposed IRBA Change and believe most audit firms, including ours, will benefit from the changes. It enhances consistency in terms of applying the PIE classification with specific focus being placed on values and thresholds of entities falling within the definition and introduces more objective criteria to be applied. Furthermore, we welcome the clarification contained in the proposed amendments to the IRBA Code to as it relates to the public interest score and public interest entity as we do see unintentional confusion of these concepts by both the public and auditors.

b) However, in general, we note the following as it relates to the revisions to paragraph R400.18 SA:

- *Harmonisation of thresholds:*
  - We support the introduction of the harmonsised thresholds, however, we believe that the CFAE should be mindful of the following potential unintended consequences:
    - As set out in our response to Question 5 below, we believe that the thresholds have not taken into consideration exchange rate fluctuations and inflation as well as other factors in the South African economy. We understand that the harmonisation of the thresholds is based on the threshold introduced previously for Pension Funds. That threshold has not been adjusted upwards to account for exchange rate fluctuations or inflation. As such, in real terms, this means that the thresholds have in fact been reduced even more than what is apparent in the amounts anticipated.
    - The consequences of the proposed revisions to paragraph R400.18 SA goes beyond independence and ethics. As set out in our response to Question 6 below, there may be unintended consequences attached to the increased number of PIEs introduced because of the introduction of the IRBA Rules, being Mandatory Audit Firm Rotation (MAFR) and the proposed IRBA Rules Arising from the International Standards on Quality Management.
    - The revisions to paragraph R400.18 SA which has resulted in

incorporating an increased number of PIEs, should be based on risks to public interest and should therefore be linked to underlying risk and exposure. It is unclear from the explanatory memorandum as to how the Committee for Auditor Ethics (CFAE) has considered this. In addition, our firm does not believe that such a link can be explicitly made.

- We do believe that consideration should be given to whether it is indeed intended for so many more entities to be PIEs and as a result to be in scope for MAFR and other consequences.

- *Overlap of entities:*
  - Based on the categorisation of each sub-paragraph anticipated in paragraph R400.18 SA, there are several instances where there are overlaps between the entities included in various categories.
  - For example:
    - Certain asset managers anticipated in sub-paragraph R400.18 SA (k) may also be a licensed central securities depository as anticipated in sub-paragraph R400.18 SA (f).
    - Broker / Dealers covered by sub-paragraph R400.18 SA (m) may outsource the holding or responsibility for safeguarding of client assets to a Licensed Central Securities Depository which is covered in sub-paragraph R400.18 SA (f).
  - As a result, we believe that there should be a simplification of the descriptions of the various categories to specify exactly which entities the categorisations are intended to cover.
- *Collective Investment Schemes:*
  - A Collective Investment Scheme covered by sub-paragraph R400.18 SA (h) is not, in itself, an entity. Instead, it is a collection of underlying unit trusts.
  - Some Collective Schemes manage a large amount of unit trusts. It has been never clear if the threshold is a threshold for the entire Collective Investment Scheme or for each underlying unit trust that is managed.
  - We believe that the sub-paragraph should be clarified to indicate that the threshold applies to each individual unit trust which would be consistent with sub-paragraph R400.18 (i) relating to Pension Funds, where the threshold applies to each individual pension fund.
- *Collective Investment Schemes, Pension Fund Administrators and Financial Service Providers:*
  - Collective Investment Schemes, Pension Fund Administrators and Financial Service Providers administer or hold assets on behalf of clients.
  - It is unclear, for example, why the threshold for a Pension Fund Administrators is the same as that for individual pension funds.
  - We believe that there should be different thresholds for:
    - An individual unit trust, pension fund or other funds; and
    - A Collective Investment Scheme, Pension Fund Administrator and Financial Service Providers as a whole. This should be a higher threshold.
- *Authorised Users:*
  - The category of Authorised Users is very broad. We would suggest that the category be simplified to cover only those entities which are intended to be covered by this category.
- *Need for guidance:*
  - As mentioned above, we note some concerns that some of the categories introduced in paragraph R400.18 SA are not specific enough, need

simplification and should deal only with those entities intended to be covered.

- Our concerns relate to the following categories:
  - Paragraph R400.18 SA (h) – Collective Investment Schemes
  - Paragraph R400.18 SA (j) – Pension Fund Administrators
  - Paragraph R400.18 SA (k) – Financial Service Providers
  - Paragraph R400.18 SA (m) – Authorised Users.
- If this is not achieved by additional revisions to paragraph R400.18 SA, we believe that separate guidance will need to be developed on the application of paragraph R400.18 SA.

Question 2: Do respondents agree that public entities listed in Schedule 2 of the Public Finance Management Act No. 1 of 1999 should be identified as public interest entities?

If "No", please explain your view and suggest a way forward.

Response to Question 2

General response to Questions 2-4 of the proposed exposure draft

a) In general, and in response to questions 2-4, we support the Committee for Auditor Ethics' (CFAE) consultation with the Auditor-General of South Africa (AGSA) on the public entities that would be considered PIEs. We believe that the enhanced clarity contained in proposed paragraph R400.18 SA (b)-(d) will provide firms and registered auditors with better guidance as to which public entities are considered PIEs.

Specific response to Question 2

b) Yes, we support that the public entities listed in Schedule 2 of the Public Finance Management Act No. 1 of 1999 should be treated as public interest entities by firms. These entities include Major Public Entities that support the major operations and functions of the country including electricity, communications and transportation, which epitomises public interest.

Question 3: Do respondents agree that public entities or institutions that are authorised in terms of legislation to receive money for a public purpose with annual expenditure in excess of R5 billion or that are responsible for the administration of funds for the benefit of the public in excess of R10 billion, as at the financial year-end, should be identified as public interest entities?

If "No", please explain your view and suggest a way forward.

Response to Question 3

a) Yes, we support that public entities or institution authorised in terms of legislation to receive money for a public purpose should be treated as public interest entities.

b) In particular, we support the introduction of the thresholds in proposed paragraph R400.18 SA (d).

c) However, we do believe that paragraph R400.18 SA (d) could be made clearer as to which entities are covered by this category.

Question 4: Do respondents agree that all universities, as defined in the Higher Education Act No. 101 of 1997, should be identified as public interest entities?

If "No", please explain your view and suggest a way forward.

Response to Question 4.

a) Yes, we support that all universities, as defined in the Higher Education Act No. 101 of 1997, should be identified as public interest entities.

b) Universities, as public entities, are of strategic importance to our country and to the education of its citizens.

c) We would, however, like to clarify our view that the subsidiaries of universities would not automatically be considered PIEs as a result of the university itself being a PIE.

d) We believe that paragraph R400.18 SA (c) should be clear that subsidiaries of universities would not automatically be considered a PIE.

Question 5: Do respondents agree with the proposed harmonisation of the thresholds to R10 billion, as follows:

(i) Collective Investment Schemes, including hedge funds, in terms of the Collective Investment Schemes Control Act No. 45 of 2002, that hold assets in excess of R10 billion?

(ii) Funds, as defined in the Pension Funds Act No. 24 of 1956, that hold or are otherwise responsible for safeguarding client assets in excess of R10 billion?

(iii) Pension Fund Administrators, in terms of Section 13B of the Pension Funds Act No. 24 of 1956, with total assets under administration in excess of R10 billion?

(iv) Financial Services Providers, as defined in the Financial Advisory and Intermediary Services Act No. 37 of 2002, holding financial products or funds on behalf of clients in excess of R10 billion?

(v) Authorised users of an exchange, as defined in the Financial Markets Act No. 19 of 2012, that hold or are otherwise responsible for safeguarding client assets in excess of R10 billion?

In "No", please explain your view and suggest a way forward.

Response to Question 5

a) Yes, we do support the introduction of harmonised thresholds for Collective Investment Schemes, funds as defined in the Pension Funds Act, Pension Fund Administrators, Financial Service Providers and Authorized Users of an Exchange.

b) However, we note the following:

- The threshold of R10 billion is based on the threshold for Pension Funds which is contained in the extant IRBA Code. As a result, the threshold related to funds that hold or are otherwise responsible for safeguarding client assets has not been revised upwards to consider exchange rate fluctuation and increased inflation and other factors in the South African economy. As a result, we believe that the threshold set in the proposed amendments to the IRBA Code are too low and therefore believe that the threshold of R10 billion should be reassessed for inflation at a minimum.
- The revisions to paragraph R400.18 SA which has resulted in incorporating an increased number of PIEs, should be based on risks to public interest and should therefore be linked to underlying risk and exposure. It is unclear from the explanatory memorandum as to how the Committee for Auditor Ethics (CFAE) has fully considered this. In addition, our firm does

not believe that such a link can be explicitly made. In that regard we support that some threshold must be made to allow for an objective threshold.

- The consequences of the proposed revisions to paragraph R400.18 SA goes beyond independence and ethics. As set out in our response to Question 6 below, there may be unintended consequences attached to the increased number of PIEs introduced because of the introduction of the IRBA Rules, being MAFR and the proposed IRBA Rules Arising from the International Standards on Quality Management.
- We do believe that consideration should be given to whether it is indeed intended for so many more entities to be PIEs and as a result to be in scope for MAFR and other consequences.

Question 6: Considering the proposed thresholds outlined in question 5 above, are respondents aware of entities that could fluctuate from being a public interest entity to not being a public interest entity, and vice versa, from one year to the next, as a result of fluctuations in the values to which the thresholds are applied, such as the value of client assets held by the entity?

If "Yes", please indicate the details and potential consequences.

Response to Question 6

a) Yes, we believe that there will be fluctuations in the number of public interest entities from one year to the next. The details and potential consequences are set out below:

- The number of PIE audit clients may change year on year, as a result of the thresholds. With the introduction of MAFR as set out in the IRBA Rule, which requires that an audit firm shall not serve as the appointed auditor of a public interest entity for more than 10 consecutive financial years, the fluctuations in number of PIE audit clients would mean that a change in the classification of an audit client from a non-PIE to a PIE would invoke the application of the MAFR Rule. Since the classification of an audit client as a PIE may change year on year, we believe that the application of the MAFR Rule in these cases will have unintended consequences. It will also require increased monitoring of audit clients to determine whether the provisions of the MAFR Rule will apply.
- The Proposed IRBA Rules Arising from the International Standards on Quality Management proposes that "An engagement quality review should be performed for all audits of financial statements of public interest entities, as defined in the IRBA Code, in addition to those engagements scoped in by ISQM 1". As a result, the fluctuation in the PIE criteria per entity would result in an increased number of engagement quality reviews, which would result in the increase in the number of engagement quality reviewers, required for audit engagements. For the wider profession, this would potentially place undue pressure on resources who are eligible to act as an engagement quality reviewer. This is particularly relevant to the proposed revision to the IRBA Code because the proposed revisions to paragraph R400.18 SA deals with those entities in specialised industries meaning that there are a limited number of engagement quality reviewers who would be eligible to perform these engagement quality reviews. We do, however, note that for our firm, our policy for engagement quality reviews already requires that an engagement quality review be performed for all PIEs and is therefore aligned to the Proposed IRBA Rules Arising from the International Standards on Quality Management.
- Based upon the recent changes in the IRBA Code, and the already increased restrictions in terms of non-assurance services that can be provided for PIE audit clients, the potential increase in the number of PIE audit clients as proposed by the revisions to the IRBA Code may further reduce the available non-assurance services that can be provided, and which also may vary from year to year.
- As some of the PIE categories are threshold based, this will require constant

verification and maintenance and monitoring of independence tools to track PIE audit clients to ensure compliance with the IRBA Code as entities may vary in classification from one year to the next and requires regular updates.

- As more entities may fall within the definition of PIE, an increased number of audit partners or reallocations of portfolios will be required to ensure adequate partner rotation takes place.

b) As a potential solution to the fluctuations in the values to which the thresholds are applied, we suggest that the values applied should be averaged over a period of three consecutive years (current year and the immediately preceding two financial years), thereby introducing some stability to the numbers used.

Question 7:
Do respondents agree with the proposed threshold of 89 000 beneficiaries for medical schemes?

If "No", please explain your view and suggest a way forward.

Response to Question 7

a) Yes, we support the proposed threshold of 89 000 beneficiaries for medical schemes, as the sector in general has seen a decline in the number of medical schemes with a limited number being the key schemes with beneficiaries in excess of 89 000.

b) In addition, we support the CFAEs consultation with the Council for Medical Schemes on the threshold to be introduced for medical schemes to be considered as public interest entities.

Question 8:
Do respondents agree that the thresholds set in paragraph R400.18 SA will allow for a consistent application of the Code and are appropriate?

If "No", please explain your view.

Response to Question 8

a) Yes, we do support the thresholds set in paragraph R400.18 SA as this would promote a more consistent application of the IRBA Code as it relates to PIEs.

b) We believe that the introduction of the thresholds will introduce objective criteria to be applied..

Question 9:
Do respondents propose any other types of entities that should be included in paragraph R400.18SA?

If "Yes", please provide details and an explanation to support the response.

Response to Question 9

a) We do not propose any other types of entities that should be included in paragraph 400.18 SA. However, we believe that certain categories of entities should not be considered PIEs at all, as follows:

- *R400.18 SA (j) – Pension Fund Administrators:*
    - There are many types of administrators in the industry, for example, Unit

Trusts Administrators and Asset Administrators. As such, it is unclear why Pension Fund Administrators have been singled out to be considered as PIEs.

- We note that if a Pension Fund Administrator is an administrator of a single pension fund with total assets under administration in excess of R10 billion, that Pension Fund Administrator would be considered a PIE. Based on this, we do not believe that this would necessarily be in the public interest to consider the Pension Fund Administrator a PIE.
- In addition, Pension Fund Administrators do not carry the assets under administration on their balance sheets, instead they only earn revenue from the assets under administration. As a result, the auditor would not need to audit the assets of the Pension Funds. We fail to see how, when performing an audit of a Pension Fund Administrator, requiring an engagement quality review would add any value or address any risks given the routine nature of the transactions and balances in the financial statements.
- Pension Fund Administrators are different to entities considered in paragraph R400.18 SA (f) who are fundamental to the operations of the markets. We fail to see how Pension Fund Administrators, who only manage underlying assets, would be considered a PIE given that our audit does not extend to the assets.
- We therefore believe that Pension Fund Administrators should be deleted from paragraph R400.18 SA of the IRBA Code.

- *R400.18 (k) – Financial Service Providers*
  - Financial Service Providers are not responsible for the custody or administration of assets under management, nor do they carry any of the underlying assets on their balance sheets.
  - We interpret R400.18 (k) to mean that the entities anticipated to be included in this paragraph would be those who are required to report in terms of section 19(3) of the Financial Advisory and Intermediary Service Act. This would mean that Nominee Companies would be applicable.
  - Nominee Companies are simply dormant companies with no income or expenses, and which exist only to hold assets on behalf of clients of its sponsoring entity. As such, we fail to see how Nominee Companies should be considered PIEs which would be required to have an engagement quality review. We believe there is no benefit to requiring an engagement quality review. There will not be any reduced risk in the marketplace by introducing an engagement quality review or any other requirements attached to being considered a PIE.
  - We therefore believe that Financial Service Providers should be deleted from paragraph R400.18 SA of the IRBA Code.

Question 10: Do respondents agree with the proposed definition of a publicly traded entity?

If “No”, please explain your view.

Response to Question 10

a) Yes, we do support the proposed IRBA Code definition of a publicly traded entity.

b) We believe that the wider definition will incorporate appropriate entities to be considered as PIEs.

Question 11: Do respondents agree with the proposed effective date?

If “No”, please indicate the reason for the disagreement, and also suggest an effective date and transitional provisions that will be more appropriate.

Response to Question 11

a) Yes, we do support the proposed effective date.

b) We believe that it will provide sufficient time for our firm to prepare for the effective date.

c) It should be noted that the work that will be required to be performed by our firm in the preparation of the revisions to the IRBA Code will include, but is not limited to the following:

- Re-categorisation of audit clients as PIEs and non-PIEs.
- Plan for, determine and action the rotation of audit clients who now meet the definition of a PIE and therefore fall in the ambit of the MAFR IRBA Rule.